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No. 85-1610

IN THE
Supreme Court of the United States
OCTOBER TERM, 1985

NORTHERN INDIANA PUBLIC SERVICE COMPANY,
Appellant,

v.

CITIZENS ACTION COALITION OF INDIANA, INC., *et al.*,
Appellees.

ON APPEAL FROM THE SUPREME COURT OF INDIANA

APPELLANT'S REPLY TO BRIEF IN OPPOSITION TO JURISDICTION

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Appellees urge the Court to dismiss this appeal either (1) because the federal questions were not timely or properly raised and were not expressly passed on, or (2) because the appeal does not present a substantial federal question. See Rule 16.1(b).

ARGUMENT

1. *The federal questions were timely and properly raised.*

It cannot seriously be maintained that NIPSCO's federal constitutional claims were not "brought to the attention of the state court with fair precision and in due time." *New York ex rel. Bryant* v. *Zim-*

merman, 278 U.S. 63, 67 (1928). NIPSCO specifically argued to the Indiana Supreme Court that precluding recovery of Bailly's costs would violate both the due process clause of the Fourteenth Amendment and the Fifth Amendment's protection against uncompensated takings of private property for public use. See J.S. 7 & n.8.[1] Because NIPSCO had raised these claims in its petition for rehearing in the Court of Appeals, these claims were properly before the Indiana Supreme Court, pursuant to Ind. R. App. P. 11(B). See J.S. 6 n.4.[2] The fact that Justice DeBruler ignored NIPSCO's federal constitutional claims in his opinion for the Indiana court's majority does not defeat this Court's jurisdiction over NIPSCO's appeal. *E.g.*, *Martinez* v. *California*, 444 U.S. 277, 282-83 n.6 (1980).[3]

Appellants cite *Cleveland Electric Illuminating Co.* v. *Office of Consumers' Counsel*, 455 U.S. 914 (1982),

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[1] Appellees themselves set out the pertinent portion of NIPSCO's brief in the Indiana Supreme Court (Opp. 17 n.8), although they omit its express reliance on the Fifth Amendment and its final paragraph.

[2] Appellees note that NIPSCO raised its federal claims for the first time "only after it had lost in the Court of Appeals" (Opp. 17 n.8). But Indiana law provides that an issue is properly before the Indiana Supreme Court on transfer if, as in this case, it was "set forth in the petition for rehearing in the Court of Appeals." Ind. R. App. P. 11(B).

[3] Appellees incorrectly assert that none of the five justices of the Indiana Supreme Court even adverted to NIPSCO's federal constitutional claims (Opp. 19). Justice Prentice, joined by Chief Justice Givan, dissented on the ground that denying a utility recovery of prudently incurred costs is "confiscatory" (App. 34a). Cf. *Webb* v. *Webb*, 451 U.S. 493, 495 (1981).

as an example of an appeal raising issues similar to those raised here, which this Court dismissed "for want of a properly presented federal question" (Opp. 13-14). There, as here, the state court did not expressly pass on the federal questions raised in this Court. But unlike NIPSCO, the appellant in that case had not raised the federal question in the state court.[4] Because NIPSCO, as explained above, timely and properly raised its federal constitutional claims in the Indiana Supreme Court, those questions are properly presented here.

2. ***The questions are substantial.***

(a) ***Takings Clause.***

Appellees argue that NIPSCO's Taking Clause claim is not substantial because NIPSCO did not show that its directors cancelled Bailly because they believed that further expenditures on the project would be disallowed as imprudent (Opp. 2 n.1). Appellees also argue that the state cannot be said to have effected any taking because it was regulatory delay at the NRC that forced Bailly's cancellation (Opp. 11). These arguments are unsound.

NIPSCO did not have to offer proof that its directors cancelled Bailly to avoid disallowance of further expenditures on the project. It is a commonplace of public utility regulation that imprudently incurred expenditures will be disallowed. NIPSCO had determined by August 1981 that further expendi-

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[4] The appellant in *Cleveland Electric* sought to avoid dismissal here by arguing that one of the appellees, in a subsequent phase of the same proceeding, had described the Ohio Supreme Court's decision as having passed on the federal constitutional issues. Reply Brief of Appellant 2-3.

tures in connection with Bailly would be imprudent. The consequences of proceeding with Bailly after it had ceased to be a prudent enterprise were obvious—so obvious, in fact, that one of the main disputes before the PSCI on NIPSCO's rate request was precisely *when* continuing with Bailly had become imprudent.[5] NIPSCO had no reason to cancel Bailly *except* to avoid incurring costs that would be disallowed as imprudent.

Appellees' contention that the state did not effect any "taking" here because Bailly's cancellation was forced by regulatory delays at the federal level is also misconceived. NIPSCO could have proceeded with Bailly in spite of those delays if it could have counted on recovering the project's costs even after those delays had rendered the project imprudent. But recovery of such costs is not allowed. It was the fact that state law precluded NIPSCO from recovering Bailly's costs after the project lost its promise of economical power that forced Bailly's cancellation and it was this forced cancellation that constituted the taking. It is the state's denial of compensation for this taking, by virtue of the Indiana court's construction of state law, that offends the Takings Clause.

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[5] The Utility Consumer Counselor, who supported NIPSCO's rate request in principle, argued that further expenditures on Bailly became imprudent at the end of 1979, when (according to the Consumer Counselor) Bailly's promise of economical power evaporated. He argued that NIPSCO should accordingly be denied recovery of its post-1979 Bailly costs. The PSCI disagreed, finding that NIPSCO had reasonably concluded that Bailly's promise of economical power had evaporated in August 1981, and thus that NIPSCO should be allowed recovery of its Bailly costs through that time. See App. 63a-65a.

(b) *Due Process.*

Appellees also argue that NIPSCO's due process claim is not substantial, principally because (they say) this Court should not concern itself with "the details of state utility regulation and ratemaking methodology" (Opp. 11, 12). They argue that the so-called "used and useful" basis for allowing recovery of costs incurred by a public utility is "firmly embedded" in this Court's constitutional jurisprudence (Opp. 20). Again, appellees' arguments cannot withstand scrutiny.

NIPSCO has not asked this Court to concern itself with "the details of state utility regulation and ratemaking methodology." NIPSCO's due process claim goes instead to the constitutional foundation of public utility regulation, and has nothing to do with "details" or "method." See J.S. 11-12. The issue is whether a state may preclude a public utility from recovering its prudently incurred costs—in particular, costs prudently incurred on a power project that the utility undertook to meet a statutory mandate to serve but was subsequently forced to cancel by operation of state law. Deciding this issue entails no "abusive and intrusive" intervention by the federal judiciary into matters of state concern (Opp. 19), but rather enforcement of basic constitutional norms. The issue presented here is simply not of the type that this Court forswore deciding in *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944).

Appellees also claim that this Court has embraced the principle that a public utility's property must be "used and useful" before the utility is constitutionally entitled to recover the costs of that property (Opp. 19-21). But this Court has never suggested that a

public utility may be required to absorb costs that it prudently incurred to meet its statutory mandate to serve, simply because those costs were incurred in connection with a project cancelled before completion.[6] The cases of this Court do not sanction such a result. A state's decision to permit recovery after rather than before a project's completion *is* undoubtedly an issue of "method," which cannot give rise to a constitutional objection. See J.S. 11. But a state's decision not to permit any recovery of a utility's prudently incurred costs—*at any time*—has never received this Court's approval.[7]

It is because public utility commissions in the overwhelming majority of jurisdictions that have con-

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[6] Nor did the D.C. Circuit suggest such a result in *Jersey Central Power & Light Co.* v. *FERC*, 730 F.2d 816 (D.C. Cir. 1984), *vacated*, 768 F.2d 1500 (D.C. Cir. 1985), quoted by appellees at page 20 of their Opposition. There, the Court of Appeals held (in an opinion it has since vacated) that a public utility was not entitled to earn a return on the cost of a cancelled power plant—that is, to include the plant's costs in the utility's rate base. Here, NIPSCO seeks only to recover Bailly's costs, not to earn a return on them.

[7] Appellees rely on *Smyth* v. *Ames*, 169 U.S. 466 (1898), but the issue in *Smyth* was not whether a utility's property had to be "used and useful" before the utility was entitled to recover its cost, but how the utility's property was to be valued for rate-base purposes—to permit the utility to show a profit, or on the basis of its "fair value." *Id.* at 543-44. The "fair value" principle embraced by the Court in *Smyth* was renounced by the Court a half-century later in *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 601-03 (1944); *id.* at 606 (Black, J., concurring). See J. Bonbright, *Principles of Public Utility Rates* 163-65 (1961). The two other cases to which appellees refer—*McCardle* v. *Indianapolis Water Co.*, 272 U.S. 400 (1926), and *Des Moines Gas Co.* v. *City of Des Moines*, 238 U.S. 153 (1915)—applied the *Smyth* rule. Neither involved the issue presented here.

fronted this issue have permitted recovery [8]—not because NIPSCO's position here lacks support—that NIPSCO cannot cite any cases of this Court in direct support of its position (see Opp. 11). We are not aware of any case prior to *Cleveland Electric Illuminating Co.* v. *PUC*, 4 Ohio St.3d 107, 447 N.E.2d 746, *appeal dismissed*, 464 U.S. 802 (1983), in which a public utility was denied recovery of prudently incurred costs of a project cancelled prior to completion; and we believe that this is because it has been firmly understood since *Hope* that rates, to be reasonable and just, *must* permit recovery of costs "properly incurred." *Mississippi River Fuel Corp.* v. *FPC*, 163 F.2d 433, 437 (D.C. Cir. 1947) (Prettyman, J.).

Appellees suggest that the emerging split among federal and state courts to which we called the Court's attention (J.S. 12-13 & n.11) is a figment of our imagination (Opp. 13). But the Wisconsin Supreme Court squarely held that it would be "arbitrary and capricious" for a state to deny a utility recovery of prudently incurred costs; the Missouri Supreme Court has avoided construing a statute in such a manner in order to avoid the "constitutional questions * * * presented" by such an approach; and Judge Wilkey—far from being a "lone, and inaccurate voice," as appellees would have it (Opp. 21)—stated the rule observed by the overwhelming majority of jurisdictions throughout the nation, from which first the Ohio Supreme Court, and now the Indiana Supreme Court, have strayed: "[U]nder the due process clause * * * no public utility [may] be com-

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[8] See J.S. 4 n.3 and Rogers & Gray, *State Commission Treatment of Nuclear Plant Cancellation*, 13 Hofstra L. Rev. 443, 452-53 & n.74 (1985) (NARUC survey).

pelled to absorb its own costs and not pass them on the consumer." *PSC* v. *FPC*, 467 F.2d 361, 370 (D.C. Cir. 1972) (Wilkey, J.).

The time is now ripe for this Court to confront the questions presented by NIPSCO's appeal.

CONCLUSION

For the foregoing reasons and for the reasons set forth in the jurisdictional statement, probable jurisdiction should be noted. Alternatively, the appeal papers should be treated as a petition for certiorari and a writ should issue.

Respectfully submitted,

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